

Message Text

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ACTION ARA-14

INFO OCT-01 ISO-00 FEA-01 ERDA-05 AID-05 CEA-01
CIAE-00 COME-00 DODE-00 EB-08 FPC-01 H-01 INR-07
INT-05 L-03 NSAE-00 NSC-05 OMB-01 PM-05 USIA-06
OES-07 SP-02 SS-15 STR-05 TRSE-00 ACDA-12 PA-01
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FM AMEMBASSY QUITO
TO SECSTATE WASHDC 6094
INFO AMCONSUL GUAYAQUIL

C O N F I D E N T I A L QUITO 7239

E.O. 11652: GDS
TAGS: BDIS EINV ENRG EC
SUBJ: NORTHWEST COMPANY HOLDS MAKE-OR-BREAK DISCUSSIONS WITH GOE
RE GULF OF GUAYAQUIL GAS PROJECT

REF: QUITO 7088

1. SUMMARY: NORTHWEST (NW) REPRESENTATIVES MET WITH GOE OFFICIALS OCTOBER 13, AND 17. NW INSISTED THAT USE OF THE GULF-OF-GUAYAQUIL GAS FOR PRODUCTION OF UREA AND AMMONIA WOULD BE UNPROFITABLE, AND THAT THE ONLY FEASIBLE USE IN THE FORESEEABLE FUTURE WOULD BE FOR ENERGY PRODUCTION. THE GOE APPEARED MORE AMENABLE TO THAT VIEW THAN PREVIOUSLY, BUT GAVE NO DEFINITIVE RESPONSE, AND INDICATED IT MAY WISH TO COMMISSION A STUDY BY AN OUTSIDE CONTRACTOR BEFORE DECIDING. NW TOLD EMBOFFS THAT IF THE GOE DOES NOT DECIDE BY MID-JANUARY EITHER TO AUTHORIZE USE OF THE GAS FOR ENERGY PRODUCTION OR TO COMMISSION A STUDY, NW AT THAT TIME WILL "WALK AWAY FROM ECUADOR", THEREBY WRITING OFF THE \$3 MILLION-PLUS THAT NW HAS INVESTED HERE AND PROBABLY FORFEITING A 1.6. MILLION PERFORMANCE BOND. END SUMMARY.

2. NW VICE PRESIDENT GLENN NELLEUN ACCOMPANIED BY TWO
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OTHER NW EXECUTIVES FROM THE US. AND LOCAL REPRESENTATIVE LUIS SALAZAR, MET WITH MINISTER SEMBLANTES AND OTHER OFFICIALS OF THE NATURAL RESOURCES MINISTRY ON OCTOBER 13 AND 17. NELLES AND SALAZAR LATER ON OCTOBER 17 TOLD EMBOFFS (E/C COUNSELOR AND PETROLEUM OFFICER) NW HAD FIRMLY INSISTED TO THE GOE OFFICIALS THAT A UREA/AMMONIA (U/A) PLANT PRODUCING 365,000 TONS A YEAR, AS ENVISAGED IN THE

NW-CEPE CONTRACT, WOULD BE SEVERELY UNPROFITABLE. THE ECUADOREAN MARKET WOULD TAKE LESS THAN 80,000 TONS A YEAR; THE BULK OF THE U/A OUTPUT WOULD HAVE TO BE SOLD ABROAD, AT PRICES CURRENTLY AND PROSPECTIVELY TOO LOW TO PERMIT A REASONABLE RETURN ON THE ESTIMATED \$180 MILLION INVESTMENT FOR THE U/A PLANT. THIS PROBLEM COULD NOT BE RESOLVED BY BUILDING A SMALLER PLANT MAINLY FOR SALES IN ECUADOR, NELLES TOLD EMBOFFS, BECAUSE AT THAT SCALE EFFICIENCY OF PRODUCTION WOULD BE UNACCEPTABLY LOW.

3. THE NW REPRESENTATIVES TOLD THE GOE OFFICIALS THAT THE ONLY FEASIBLE USE FOR THE GAS IN THE FORESEEABLE FUTURE WOULD BE FOR PRODUCTION OF ELECTRICAL AND THERMAL ENERGY FOR MUNICIPALITIES AND INDUSTRIES IN THE AREAS OF GUAYAQUIL AND MACHALA. THEY POINTED OUT THAT MANY INDUSTRIES IN THOSE AREAS ARE ALREADY EQUIPPED TO USE GAS IN LIEU OF THE PETROLEUM DERIVATIVES CURRENTLY USED. COSTS OF CONVERSION TO GAS FOR OTHER USERS WOULD BE SLIGHT. SINCE THE GOE SUBSIDIZES DOMESTIC PRICES OF PETROLEUM DERIVATIVES, THE PROPOSED CONVERSION TO GAS WOULD SAVE THE GOE ITSELF AT LEAST \$18 MILLION A YEAR.

4. WHEN THE GOE OFFICIALS IN RESPONSE ASSERTED THAT THE MINISTRY'S OWN STUDIES AND SHOWN U/A SALES ABROAD WOULD BE PROFITABLE, AND THAT USE OF THE GAS FOR ENERGY WOULD BE MORE COSTLY THAN USE OF PETROLEUM DERIVATIVES, NELLES
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REQUESTED A COPY OF THOSE STUDIES; BUT HE WAS TOLD THEY WERE ONLY FOR THE MINISTRY'S USE. NELLES OPINED TO THE

EMBOFFS THAT IN FACT THERE ARE NO SUCH STUDIES. HE SAID THE MINISTRY HAS MERELY BEEN RELYING ON SKETCHY REPORTS BY SOME OF ITS UNQUALIFIED PERSONNEL WHOSE INFORMATION HAD BEEN OBTAINED MAINLY FROM COMPANIES EAGER TO SELL THE EQUIPMENT THAT WOULD BE NEEDED FOR THE U/A PLANT, RATHER THAN FROM PARTIES ACTUALLY ENGAGED IN INTERNATIONAL MARKETING OF U/A. THE GOE'S UNREALISTIC VIEWS HAVE ALSO DERIVED, NELLES ASSERTED, FROM ADVICE THAT WAS BEING GIVEN TO THE MINISTER BY CEPE'S RECENTLY-FIRED DIRECTOR OF INDUSTRIALIZATION, MARIO PAZ, WHO IN CONJUNCTION WITH FORMER CEPE DIRECTOR COL. LUIS PINEIROS HAD BEEN ACTIVELY SEEKING KICKBACKS FROM PROSPECTIVE SUPPLIERS OF EQUIPMENT FOR THE U/A PLANT. NELLES SAID NW'S CONSTLY IN-HOUSE STUDY OF ECUADOR'S U/A PROSPECTS LEFT NO DOUBT THAT PRODUCTION AS PER THE CONTRACT WOULD BE FINANCIALLY DISASTROUS FOR NW AND THE GOE.

5. NELLES SAID THAT IN THE DISCUSSIONS MINISTER SEMBLANTES FOR THE FIRST TIME INDICATED THAT THE MINISTRY'S "STUDIES" MAY BE LESS THAN AUTHORITATIVE AND THAT MARIO PAZ' ADVICE

TO THE MINISTRY MAY HAVE BEEN SELF-SERVING. (PAZ WAS FIRED A FEW WEEKS AGO APPARENTLY BECAUSE SOME OF HIS HANKY-PANKY HAD COME TO LIGHT.) THE MINISTER TOLD NELLES THAT THE MINISTRY WILL GIVE FURTHER THOUGHT TO NW'S PROPOSAL AND WILL GIVE A RESPONSE SHORTLY. HE SAID THE MINISTRY MAY WISH TO COMMISSION AN OUTSIDE CONTRACTOR TO PREPARE A COMPREHENSIVE FEASIBILITY STUDY. NELLES TOLD THE EMBOFFS THAT UNDER THE NW-CEPE CONTRACT THE COST OF SUCH A STUDY, WHICH PROBABLY WOULD BE ABOUT \$250,000, WOULD HAVE TO BE BORNE ENTIRELY BY THE GOE.

6. NELLES TOLD THE EMBOFFS THAT NW'S PATIENCE IS RUNNING OUT. IF THE GOE DOES NOT AGREE WITHIN 90 DAYS--I.E., BY MID-JANUARY--TO USE THE GAS FOR ENERGY PRODUCTION, OR TO
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COMMISSION A FEASIBILITY STUDY, NW WILL "WALK AWAY FROM ECUADOR", HE DECLARED. THE COMPANY WOULD WRITE OFF THE SOMEWHAT MORE THAN \$3 MILLION IT HAS SO FAR INVESTED IN THE UNDERTAKING, AND WOULD STAND TO FORFEIT ITS \$1.6 MILLION PERFORMANCE BOND, ALTHOUGH REGARDING THE BOND NW WOULD SUE IN THE ECUADOREAN COURTS TO PREVENT FORFEITURE, ON THE GROUNDS THAT NW'S NON-PERFORMANCE WOULD HAVE BEEN NON-VOLUNTARY. HE UNDERScoreD THAT NW WILL NOT PROCEED WITH THE PROJECT UNLESS AND UNTIL IT IS ASSURED THAT THERE WILL BE A PROFITABLE MARKET FOR THE OUTPUT OF NATURAL GAS.

7. NELLES MENTIONED NW'S EXPECTED HUGE CONTRACT FROM THE USG FOR SUPPLYING GAS FROM ALASKA TO THE US. AS EVIDENCE THAT NW HAS OTHER FISH TO FRY. HE EXPRESSED IRRITATION OVER THE FREQUENT CHARGES BY ECUADOREAN POLITICIANS THAT NW IS LITTLE MORE THAN A "PAPER" COMPANY AND THAT NW HAS SEVERE FINANCIAL PROBLEMS.

8. THE NW REPS ASSERTED THAT NW HAS IN NO WAY DEFAULTED ON ITS CONTRACTUAL OBLIGATIONS. THE REQUIREMENT FOR NW TO DRILL A SPECIFIED NUMBER AND AREA OF WELLS NEED NOT BE FULFILLED UNTIL THE TERMINATION OF THE FIVE-YEAR CONTRACT IN APRIL 1980. NW'S OBLIGATION UNDER THE GOE HYDROCARBONS LAW NOT TO SUSPEND EXPLORATION ACTIVITIES FOR MORE THAN SIXTY DAYS IS BEING MET, NELLES SAID, SO LONG AS NW PERSONNEL AND EQUIPMENT ARE PHYSICALLY IN THE CONCESSION AREA, AS IN FACT THEY ARE.

9. NELLES AND HIS US. COMPANIONS DEPARTED QUITO ON OCTOBER 18, AFTER LEAVING WORD WITH THE GOE THAT THEY WOULD BE PREPARED TO RETURN AND RESUME DISCUSSIONS FROM AROUND OCTOBER 28.

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10. EMBASSY COMMENT: IT IS DIFFICULT TO SEE HOW THE GOE
COULD DO ANYTHING BUT GO ALONG WITH NW, WITH OR WITHOUT
HAVING COMMISSIONED AN OUTSIDE STUDY FIRST. OUR CONTACTS
IN OTHER EMBASSIES HERE TELL US THAT THE GOE IN THE PAST
YEARS HAS APPROACHED VARIOUS NON-US COMPANIES, NONE OF WHICH,
HOWEVER, WERE WILLING TO TAKE ON NW'S
CONTRACT.
BLOOMFIELD

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Message Attributes

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Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 22 May 2009
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Enclosure: n/a
Executive Order: GS
Errors: N/A
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